MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2016/2017

BAC2664 – AUDITING

(All sections / Groups)

12 October 2016
9 a.m – 12 p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This question paper consists of 4 pages with 5 questions only (excluding cover page).
2. Attempt ALL FIVE questions. All questions carry equal marks and the distribution of the marks for each question is given.
3. Please write all your answer in the Answer Booklet provided.

Question 1

(a) Mawar Store is a retailer of ladies' clothes and accessories. Customers select the menu from the catalogue available at the shop. The catalogue provides a product description, picture and price for all products available for sale. Customers just choose the product they wish to purchase and inform the staff at the counter. The following are internal controls Mawar Store has established for its sales:

i. Only products shown on the catalogue can be purchased. Other company's products not shown on the catalogue are unavailable for sale.

ii. The catalogue sales system is linked to the perpetual inventory system that verifies quantities on hand before processing the sale.

iii. Before the sale is authorized, Mawar Store obtains credit card authorization codes electronically from the credit card agency.

iv. Before the sale is finalized and payment made, the staff at the counter will confirm the product name, description, unit price and total sales price for the transaction.

Required:

(1) For each control, identify the transaction related audit objective(s) being fulfilled if each control is in effect. (3 marks)

(2) For each control, describe potential financial misstatements that could occur if the control was not present. (6 marks)

(b) i. Distinguish between management and the auditor's responsibilities for the financial statements being audited. (3 marks)

ii. Define the management assertion related to financial statements. Identify five broad categories of management assertions. (6 marks)

iii. Explain the role of the auditor with respect to the Malaysian Code on Corporate Governance. (2 marks)

(Total 20 marks)

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Question 2

(a) Engagement letter is an important document prepared by the external auditor in the 'Accept client and perform initial audit planning' stage. This stage is the first stage in the process of planning the audit. Explain the objectives of preparing this letter and the contents of this letter. (14 marks)

(b) Persuasiveness of evidence have two characteristics which are *appropriateness* and *sufficiency*. Define *appropriateness* and *sufficiency* of evidence. (6 marks)

(Total 20 marks)

Question 3

Rizal is the auditor of the Reema Industries Bhd. He is considering the audit work to be performed in the accounts payable area for the current year engagement.

The prior year working papers show that confirmation requests were mailed to 200 of Reema's 2,000 suppliers. The selected suppliers were based on Rizal's samples, which was designed to select accounts with large balances. A substantial number of hours were spent by Reema and Rizal in resolving relatively minor differences between the confirmation replies and Reema's accounting records. Alternative audit procedures were used for suppliers who did not respond to the confirmation requests.

Required:

(a) Discuss the accounts payable audit objectives that Rizal must consider in determining the audit procedures to be followed. (6 marks)

(b) Discuss situations in which Rizal should use accounts payable confirmations, and discuss whether Rizal is required to use them. (7 marks)

(c) Discuss why the use of large-value balances as the basis for selecting accounts payable for confirmation might not be the most efficient approach, and indicate the more efficient procedures that could be used to select accounts payable for confirmation. (7 marks)

(Total 20 marks)

Question 4

(a) The directors of Adibah Sdn. Bhd., have accused their auditor of disclosing certain financial information of the company to their bankers, without their approval. Under this circumstance, the current auditor has indicated their intention to resign. Your firm has been nominated to replace the existing auditor.

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Required:

Advise the directors on the procedure for appointment of an auditor to fill the casual vacancy as stipulated by the Companies Act, 1965.

(6 marks)

(b) 'Understand the client's business and industry' stage is one of the processes involved in planning the audit. Explain three primary reasons for obtaining a good understanding of the client's business and industry. (6 marks)

(c) Distinguish between errors and fraud. What are the auditor's responsibility for finding each? (8 marks)

(Total 20 marks)

Question 5

(a) For each of the following independent situations, indicate the reason for and the type of auditors' report that you would issue. Assume that each item is significant.

(i) You have been appointed as an auditor for Marlene Bhd the holding company and its subsidiaries. One of the subsidiary's financial statements was qualified by their auditor. (2 marks)

(ii) Your client has incurred substantial losses in recent years and is unable to repay various bank loans which are falling due. The company's ability to continue as a going concern is in doubt. (2 marks)

(iii) During your audit of Andrea Sdn. Bhd. the financial controller refuses to allow you to confirm accounts receivable because he is concerned about complaints from the customers. You are unable to satisfy yourself about accounts receivable by other audit procedures. (2 marks)

(iv) You are auditing a pharmaceutical company and it was later found that the company is a defendant in a lawsuit involving a breach of contract. The legal counsel of the company indicates that the company is likely to be liable, but the company does not want to disclose this information in the financial statements. (2 marks)

(v) Kenny Bhd. has used the reducing-balance method to depreciate its machinery. During the current year, the company switched to the straight-line method because they felt that it better represented the utilisation of the assets. You agree with their decision. All information is adequately disclosed in the financial statements. (2 marks)

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(b) There are two common types of confirmations used for confirming accounts receivable: "positive" confirmation and "negative" confirmation. Distinguish between both types of confirmation and state the circumstances in which each should be used. Why do auditors often use a combination of positive and negative confirmations on the same audit?

(10 marks)

(Total 20 marks)

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